

FILE COPY

USAID MAY 2 7 1999 RIGA Londor Prague Budapes Warsaw Sofie Moscow Tashken Almate Jakarte Melbourne Mexico Cite San Salvado

April 26, 1999

Ms. Cathy Toth
COTR
C/O Mr. Bill Penoyar

USAID ENI/PER/POD, RRB, Suite 2.06 Ronald Reagan Building 1300 Pennsylvania Avenue, N.W. Washington, D.C. 20523-0039

USAID Riga, Latvia			
ACTION	4 · · · · · · · · · · · · · · · · · · ·		
INFO	06/04		
DATE			
FILE	Bank Sup Rep		

RE: Bank of Latvia: Strengthening Bank Supervision, Phase III Contract #EPE-I-05-95-0048-00 - Task Order #5

Final Report March 31, 1999

Also intended to meet Quarterly Reporting Requirements for the three months ended March 31, 1999

Dear Cathy:

The Final Report for the above noted Task Order is enclosed for your review. Our technical assistance program ended March 31, 1999. The Report and the enclosed Attachments summarize the significant achievements realized by the Bank of Latvia (BOL) under this USAID technical assistance program.

The Technical Assistance program commenced in early 1995 under a separate USAID funding vehicle. This Task Order commenced February 1996 as a follow-on to the prior work. As the Report indicates, this Task Order was modified in mid-1997 to incorporate the use of short term advisors, in contrast to previous resident advisors, on an as needed basis. This decision was made given the progress of the Bank of Latvia supervisory function and USAID's desire to 'graduate' the Bank from a resident program.

The decision proved to be successful. Periodic guidance was provided to the Bank staff on an as needed basis and ongoing contact with BOL personnel and the advisors continued. Additionally, advanced training both in-country and in the U.S. were provided to several individuals. Overall, Barents has met the overall objectives of the



Task Order and complied with the Tangible Results and Benchmarks as required. Detailed information on our progress over the term of the contract is provided in the periodic Quarterly and Monthly reports*.

We have enjoyed the opportunity to assist USAID in achieving its objectives of strengthening the overall financial markets through the enhancement of banking supervision. We wish to acknowledge the support of all involved from both USAID and the Bank of Latvia. If you have any questions regarding this project, please contact me at (202) 331 - 4549.

Very truly yours,

Barents Group, LLC

Lori Bittner Yerzyk

Financial Sector Regulatory Practice

Lei Bother Yerzyle

Director

Attachment

cc:

Ms. Cathy Toth, USAID - DC
Mr. Howard Handler, USAID-Riga, Latvia
USAID Directorate for Policy (2 copies)
World Bank Operations Officer- Latvia

Advisor - Woolford

Project File

[*Note: Commencing mid 1998, only Quarterly Reports were submitted to USAID. The elimination of formal Monthly Reports was done at the request of the COTR/CTO.]

Barents Group LLC a KPMG Peat Marwick Company

Bank of Latvia: Strengthening Credit Institution (Bank) Supervision, Phase III Final Report

Also includes information as required by the Quarterly Report for the Period of January 1999 – March 1999

Project # 1100-005 Contract # EPE-I-05-95-00048-00 Task Order #5 Name of Contracting Officer's Technical Representative (COTR): Ms. Catherine Toth

Prepared by Lori Bittner Yerzyk, Project Manager With information provided by Advisors Woolford, Ballinger, and Clarke

April 1999

Background

This technical assistance program, which commenced February 1, 1996 is being carried out in accordance with the Task Order referenced on the cover page. The team structure consisted of:

Washington, DC Lori Bittner Yerzyk, Project Manager

Riga, Latvia
Kathryn Woolford, Short Term Advisor
Robert Clarke, Senior Policy Advisor
Short Term Advisors- C. Dale Wilson, Dorothy Fusco, Susan Ballinger

The objectives for the Task Order are to assist the Credit Institution Supervision Department of the Bank of Latvia:

- (1) to strengthen and refine its supervision and monitoring capabilities;
- (2) to develop efficient and appropriate enforcement mechanisms; and
- (3) to develop the procedures to deal with problem banks, including liquidation techniques.

The Task Order has had three formal modifications since commencement. Modification No. 1 enabled our Resident Advisor to continue her efforts of implementing an effective banking supervision culture. The purpose of Modifications 2 & 3 were intended to allow us to provide ongoing assistance to the Bank of Latvia (post resident advisor). These modifications changed the focus of assistance to enable us to provide intermittent assistance through the use of short term experts and by providing advanced training to Bank of Latvia supervision staff abroad. Specifically, the modifications revised the completion date of the task order, modified the scope of work, and revised the budget and the expatriate level. [Note COTR Ms. Cathy Toth provided for a no-cost extension through September 30, 1998 subsequent to Modification No. 2.]

History

Barents Group under a USAID program has been providing assistance to the Bank of Latvia (BOL) for over three and a half years. Significant progress has been made in strengthening the capacity of the Bank Supervision Department (BSD) at the BOL. As a result of the accomplishments, it was determined that a full time resident advisor was no longer needed to provide technical expertise. Nonetheless, the BOL could benefit from a highly focused program of training and periodic visits from senior policy advisors. This type of technical assistance would help to ensure that the tools and the training that Barents Group/USAID have provided to date, continue to be used and fully entrenched in banking supervision activities. In addition, the ability of the BOL to continue to have

access to a senior policy advisor would allow for a smooth transition as the BOL/BSD moves away from a resident advisor.

Therefore, task order modifications No. 2 and No. 3 primarily allowed for specialized and advanced training both in the US and Latvia. The BOL recognized that contact with the US bank regulatory authorities and US banking methods are an effective way to raise both the skill level and understanding of issues in modern banking. In addition, this extension was also anticipated to compliment the USAID capital markets project specifically in the areas of legal/regulatory and accounting.

This Final Report will cover accomplishments since the departure of our resident advisor (mid-1997) through contract end, March 31, 1999. The 'Final Report dated June 1997' prepared by Resident Advisor Kathryn Woolford should also be reviewed in conjunction with this report to provide a more comprehensive analysis of the accomplishments achieved during this technical assistance program.

Summary of Accomplishments during the Period of Performance

The technical assistance program in Latvia is considered a success. The Bank of Latvia has created an effective and efficient banking supervisory process. The supervisory department is staff by individuals who have received training and are able to carryout the goals, mission and objectives of the Bank of Latvia.

The supervisory department has instituted a banking supervisory culture and has shown the ability to control both entry and exit into the system. Specific examples of accomplishments include:

- A comprehensive examination procedures manual has been adopted and a process is in place to periodically update the manual as necessary.
- ♦ A process has been implemented to allow for an integrated supervisory process which includes onsite and offsite examinations based on risk.
- A formal training program has been adopted which enables all of Bank of Latvia staff
 to benefit from out-of-country training. Staff members who participate in training
 must prepare documentation, share reference material, and provide a presentation to
 other staff members.
- An examiner certification process was implemented. A multi-part test has been
 developed which includes written and oral presentations. Over half of the staff has
 taken the test and passing grades were required to be certified.



- ◆ A Depositor Payout Program was initiated which enabled the BOL to efficiently resolve a large state owned failed bank.
- ♦ The Bank of Latvia initiated the translation of the International Accounting Standards 1997 and the International Standards of Auditing into Latvian and the subsequent sale/distribution throughout the country.
- A comprehensive Reference Library was created within the Bank of Latvia.

All of these accomplishments were achieved through the USAID funded program. The success is also supported by the recent request of the National Bank of Ukraine for the Latvian supervisors to assist in onsite examinations of Ukrainian banks. The Latvian supervisors were hired as consultants. This shows the respect that the Bank of Latvia has achieved within the region.

<u>Tangible Results/Benchmarks</u> <u>MODIFICATION NO. 3 [extended period of performance through March 31, 1999]</u>

Advanced Training Seminar

- 1. The contractor shall provide at least ten-selected bank supervisors at the Bank of Latvia with advanced training securities activities, including but not limited to, portfolio management and pricing for derivatives and other securities products and accounting for derivatives and other security products.
- Achieved. A capital markets expert assisted the Bank of Latvia for two weeks in January 1999. She presented case studies, assisted with current issues, and provided classroom training seminars for over 20 staff members of the bank of Latvia. Additionally, she met with representatives from USAID/Barents capital markets project. (Refer to Attachments -- Trip Report prepared by Advisor Susan Ballinger for additional details)
- 2. The above —described securities training must be presented in seminar form with case studies. Materials, which can be utilized during practical application of the materials taught, must be prepared and left with the Bank of Latvia. The contractor shall field experts with both regulatory and industry experience for the training.

Achieved. See above.

US Based Training

 The contractor shall provide U.S. based training with the Federal Reserve, OCC or other comparable bank regulatory agency for five bank supervisors from the Bank of Latvia.

Partially Met. The Bank of Latvia identified three individuals to attend training in the U.S. The three attended courses during the first quarter of 1999 in the US-Washington, DC and Texas.

MODIFICATION NO. 2 [extended period of performance through July 31, 1998]

The Tangible Results to be achieved as a result of the technical assistance as reflected in the modified Task Order are as follows:

1. Up to ten BOL staff (up to three Latvian commercial bankers can be substituted for BOL staff) will have attended an advanced banking supervision training program in the United States, which may include an internship at a U.S. bank regulatory authority or commercial bank.

Achieved. Seven Latvians traveled to the U.S. for specialty training during the period April 1998- August 1998. This included seven members from the Bank of Latvia and one commercial banker. The contractor worked closely with the BOL and the local banker's association to identify other participants, however, no names were identified. The Bank of Latvia and the banker's association indicated that they were satisfied with the number of participants selected.

Four of the participants from the BOL also participated in internships with the U.S. regulatory agencies ranging from 1-2 weeks Three of the participants met with representatives to discuss issues that related to their specialty area/position. These meetings were organized based on the individual's request and provided for an opportunity to compare ideas and to learn from the US regulators.

One BOL member was given the opportunity to participate in an onsite examination. She indicated that this experience was extremely valuable and she was able to take several ideas/documents back to the BOL for use.

2. At least three classroom training sessions will have been held for the select BOL regulatory staff on advanced topics in bank supervision and specialized issues, e.g. derivatives.

Achieved. Training was provided while in-country to select examiners/management by Advisor Kathryn Woolford and Senior Policy Advisor Robert Clarke. The BOL was unable to commit to topics for formal sessions during this and prior quarters. However, capital markets/derivatives training is planned for January 1999 with technical expert Ms. Susan Ballinger and Ms. Kathryn Woolford. (Refer to comments under Modification No. 3)

3. The bank supervision authority with the assistance of the senior policy advisor will have evaluated current activities, bank supervision practices, and prudential regulations and developed plans to modify and enhance these as the financial markets evolve.

Achieved. Mr. Robert Clarke has provided guidance to the Latvians while in-country during the 3rd quarter and also via telephone subsequently.

4. The bank supervision authority will have established a comprehensive reference library containing textbooks and periodicals on all aspects of banking/banking supervision.

Achieved during the 1st Quarter 1998.

The Tangible Results have been achieved. Some deviations were necessary to accommodate the Bank of Latvia needs. Overall, the assistance provided met the Task Order Objectives and desired Results.

Brief Summary of Activities During the Quarter

- The DC Project Manager worked closely with BOL staff to organize additional US training. Three Latvian supervisors traveled to the US to attend courses in Capital Markets or Real Estate Lending.
- Capital Markets Advisor Susan Ballinger and Advisor Kathryn Woolford traveled to Latvia to provide ongoing technical assistance. Ms. Ballinger provided classroom training in several areas (refer to Attachments) and Ms. Woolford provided assistance to Ms. Ballinger as well as working with the BOL on current issues.
- ♦ Advisor Kathryn Woolford prepared a summary report for USAID-Latvia to use as part of a final close-out synopsis. (Refer to Attachments)

--note: no benchmarks are in place for the current quarter- summarized below is our status to date in achieving the benchmarks as outlined in contract modification #2--

Progress in Achieving the Benchmarks To Date

The following Benchmarks were to be achieved auring the 4" Three Month Period (Maj-July 1998)
- The individuals participating in the advanced training will travel to the U.S. to attend classroom training and also to obtain experience as interns in either U.S. commercial banks or with regulatory agencies.
X MetUnmetPartially Met
Two Latvians participated with the FDIC on internships during onsite examinations Meetings were also scheduled with U.S. regulatory officials for Latvians in the U.S. of training.
- The individuals receiving training will have developed an outline of their educational goals to be achieved while in the U.S. which also identifies a mechanism and audience to share the experience (ie, seminars; reference material development) upon completion.
XMetUnmetPartially Met

Barents Group LLC

Latvians were chosen for training based on their experience, interest, and educational needs. The BOL has instituted a program whereby information/reference documents received while on training are shared with other staff members.

- Assistance will be provided to the BSD to develop a plan to ensure that future

 Assistance will be provided to the BSD to develop a plan to ensure that future training opportunities are identified and that ongoing educational advancement is achieved.
X Met Unmet Partially Met
The BOL is actively involved in training opportunities offered throughout the world.
The following Benchmarks were to be achieved during the 3 rd Three Month Period February 1998 – April 1998)
A corporate governance seminar with the assistance of the BSD to discuss recent initiatives in the banking community will be held.
_Met _X_UnmetPartially Met
Not desired by BOL. The proposed March visit by Senior Policy Advisor Mr. Robert Clarke was postponed upon a decision by USAID. Discussions have ceased regarding the organizing and planning of a corporate governance seminar in Latvia. Coordination with the Latvian Banking Academy and the BOL was anticipated.
9/98 Update:MetUnmetX Partially Met Mr. Robert Clarke provided in-country assistance to the BoL based on their identified needs. (See previous comments)
The final candidates to participate in the advanced training program(s) will be selected.
X MetUnmetPartially Met
Eight individuals have been nominated and confirmed to participate in U.S. based raining.
The following Benchmarks were to be achieved during the 2nd Three Month Period November 1997 – January 1998)
The first application deadline for individuals interested in participating in the advanced training program in the U.S. will be set and initial interviews conducted.
Barents Group LLC 7

X MetUnmetPartially Met					
A decision was made by the Bank of Latvia, USAID, and our advisor to revise the original application process planned for U.S. training participants. Given the desire to shift to training offered by the Federal Reserve Bank -Board of Governors, the application process was revised. Generally, individuals are now being chosen by the respective departments (ie, Bank of Latvia, Banker's Association, and Banking Institute of Higher Learning).					
- Senior policy advisor will have provided guidance to the BSD on recent issues/concerns.					
X MetUnmetPartially Met					
The senior policy advisor visited Latvia in July.					
The following Benchmarks were to be achieved during the 1st Three Month Period (August - October 1997):					
- One Bank of Latvia (BOL) inspector will travel to the U.S. for two - four weeks to participate in a bank analyses training seminar sponsored by the Federal Reserve Bank and to meet with U.S. regulatory agency officials.					
X MetUnmetPartially Met					
Achieved during the first three month period.					
- A panel will be created consisting of officials from the BOL, the Bankers Association, and/or the Latvian Bank Academy to develop a plan to evaluate and select candidates to participate in the advanced training program.					
X MetUnmetPartially Met					
See above. A panel selection process will not be used. Training participants will be chosen through recommendations. Initial recommendations have been received and their desired course of study provided.					
- A schedule for the training to be provided will be presented to USAID for approval.					
MetUnmetX_Partially Met					

Barents Group LLC

Work towards achieving this Benchmark was completed during the January 1998 visit. A list of courses for BoL staff to attend which are sponsored by the Federal Reserve Bank was drafted. The list will be presented to the Federal Reserve Bank by Project Manager Yerzyk. Also, discussions with the Bankers' Association and the Academy were held regarding potential training opportunities in the U.S. They were invited to nominate candidates for overseas training. All names and courses have/will be presented to USAID as received.

4/98 Update: X Met ___Unmet ___Partially Met A schedule for U.S. training has been developed and confirmed for eight participants. Refer to prior Monthly and Quarterly Reports for details.

Attachments

- Latvian Summary Report: Draft—1/99 prepared at the request of USAID by Ms. Kathryn Woolford
- 2. Ms. Kathryn Woolford: Trip Report 1/99
- 3. Ms. Susan Ballinger: Trip Report 1/99—Capital Markets Specialists
- 4. U.S. Training Participants: Courses Attended/Internships
- 5. Mr. Robert Clarke, Senior Policy/Legal Advisors—"Statement of Cooperation" 9/98
- 6. International Accounting Standards- Publication-Press Release
- 7. Miscellaneous News Clippings (1st Quarter 1999)
- 8. Letters of Appreciation from Latvian staff to USAID/Barents Group LLC
- 9. Latvia's Assistance to the Bank of Ukraine
- 10. Resident Advisor 1997 Final Report Excerpts dated July 25, 1997 Project
- 11. Administration: Task Order Data (included for USAID internal purposes only)

Attachment

1. Latvian Summary Report: Draft—1/99 prepared at the request of USAID by Ms. Kathryn Woolford

Summary Report Prepared by Advisor Kathryn Woolford January 1999

Purpose: This summary was prepared at the request of USAID Latvia. USAID Latvia will use this information to prepare a final close-out mission report.

DRAFT

Bank Supervision Assistance in Latvia: From Advised to Advisor

USAID assistance to the Bank of Latvia began in 1994 after a change from US Treasury to USAID. The purpose of the project was to bring the bank examination skills of the Bank of Latvia supervisors from transactions based examination practices to risked based practices. The assistance program was constructed to build from skill to skill and ended with the development of a sophisticated bank supervision department in the Bank of Latvia capable of examining banks in any environment.

At the outset of the development of the Bank of Latvia project, the supervision program took an appropriate back seat to monetary policy issues. The Senior Management of Latvia's central bank was concentrating its efforts on establishing the currency and curbing inflation. If one examines the Basle Core Principles of Bank Supervision, one will see that the primary foundation for bank supervision is a stable economic environment. In this regard, the Bank of Latvia was certainly getting off on the right foot. However, the financial community was not waiting for an orderly process in its development and while monetary policy was stabilising, the formal infrastructure so necessary to the development of a satisfactory lending process was not in place. Issues such as accounting practices, collateral law, bankruptcy laws and clear land titles were developing with support from donors but not moving fast enough to accommodate the needs of an actively lending banking system. The new Latvian commercial bankers were taking advantage of the developing market's inequities and volatilities in exchange rates while engaging in what may be considered wholesale insider abuse. Those banks which were not investing in insider interests preferred to invest in high interest rate Latvian treasury instruments or in foreign bonds, which were appeared safer than lending on the domestic market.

In the beginning, the project used a Latvian-American bank examiner who used his language skills and his experience with the New York State Bank Authority to work with the supervisors in on-site examinations. Many members of the supervisory staff did not have the academic background for bank supervision. The historic process of supervision in Latvia was transaction based supervision and these skills needed to be conveyed to the beginning examiners. were the supervisors starting out on a long program of learning and adjustment to a market based banking environment, but the country of Latvia itself was beginning this process. While risk based supervision practices are now the commonly accepted rule in most western markets, it should be noted that in the United States, transaction based examination procedures were the primary means of examination for more than one hundred years. Therefore, in a carefully constructed program, developing both the relationship between the advisors and the central bank and laying a proper foundation for risk based analysis, the USAID assistance program to the Bank of Latvia began with the basics of transactional based supervision with the new examiners on-site. As supervision activities increased and supervisors gained confidence - banks and bankers tested the waters of the new economic process.

There were two other supervision advisors provided by other donor entities during this period. One was Michael Bourke who was funded under the PHARE program and the other was funded under IMF. The central bank was receptive to assistance in bank supervision although there were serious considerations concerning the confidentiality of information from individuals and the financial system. Mr. Bourke worked with the central bank to develop a reporting accountant program similar to that used by the Bank of England and to develop the off-site surveillance system which processes were both integral in the development of an effective supervision division within the central bank.

The Latvian government took a very aggressive approach to the establishment of a private commercial banking system. By early 1994 there were more than 70 banks licensed to carry on banking activities in the country of Latvia. At the time, the concept was that more banks would generate market forces sufficient to keep banks operating in a competitive and therefore prudent manner. However, many of the bankers operating these financial institutions did not have the background to conduct safe and sound banking operations and several used the banks as their private "pocket books". As in any financial system, there were those who operated for personal gain and disregarded the supervisory efforts of the central bank. By the middle of 1996, only about 32 of these banks remained and about half of these remaining 32 were allowed to take private person deposits.

Bank Baltija

During the 1980's and early 90's, more than 100 countries experienced a banking crisis. Banking crises in the Baltics occurred in more or less a wave effect which began in Estonia and went south. During late 1994 and early 1995, several of the smaller banks failed in Latvia and depositors suffered losses. Then in May of 1995, after exhaustive efforts to remedy the situation, the Bank of Latvia was forced to remove the license of Bank Baltija, the largest bank in Latvia. This was a politically charged event which had obvious repercussions throughout the Latvian financial system. The failure was due to major insider abuse and the president and CEO of the bank were both arrested.

USAID was able to respond to the request for assistance in the form of a problem bank advisor shortly after the failure of Bank Baltija. Since this bank failed under the existing commercial bankruptcy law its resolution and liquidation was entrusted to the local economic court and an administrator, and subsequently to an accounting firm for final liquidation. However, during the court process, the advisor defined an outline for the role of the administrator and worked with the administrator in the deposit compensation program. As the development of the resolution process continued after the demise of Bank Baltija, the advisor was able to assist the supervisory department with recommendations on the role of the proxy, or special supervisor and other resolution matters.

Difficulties in attempting to remove the license of the bank and to take corrective measures were exacerbated by the lack of enforcement powers in the existing banking law. These difficulties were magnified by the political connections of the Baltija management who were successful in stalling the efforts of the central bank and able to dissipate the assets of the bank through transferring promissory notes out of the country and by creating a lien over all the remaining assets of the bank All of the assets of the bank including its furniture and fixtures were tied up in a sophisticated collateral agreement executed between the bank itself and a state owned entity.

Bank Baltija held deposits equal to approximately 25% of the broad money of

Latvia. The bank's deposits included those of many of the more prominent western companies operating in Latvia at the time. It also held over 250,000 deposit accounts reflecting the deposits of more than 140,000 individuals or about 6% of the total population of the country. Many of these depositors had been lured from the relative safety of the state owned savings bank by the attraction of extremely high interest rates paid by Bank Baltija. Many of its non-insider loans were to major industries within the Latvian business community and to the state owned enterprises, one in particular was to the state owned utility company.

That systemic risk existed was an understatement. Solvent banks which, with the removal of Bank Baltija from the system, now became the largest banks in the system, played against one another by starting rumours of trouble causing depositors to move large deposits from the already fragile system. The role of the Bank of Latvia as supervisor of financial institutions now came to the forefront. The replacement of the law on financial institutions became extremely important. While the initial intent appeared to be the imposition of three new laws, Bank Bankruptcy, Deposit Insurance, and a law on financial institutions, only the latter was passed by the Saeima late in 1995. At the same time, a new leader to the supervision department of the Bank of Latvia was named and the supervision department took on a much stronger role in the dynamics of the financial system.

Deposit Compensation

There was no deposit insurance law in effect but the Latvian Prime Minister promised the payment of a portion of the Baltija deposits. This may certainly have been politically motivated since the country's elections were due in the early fall of 1995. Suddenly there was a need to develop a deposit compensation program for a cash based society almost overnight. The USAID funded advisor with the assistance of a PHARE funded advisor developed and tested a deposit compensation program. The team made a presentation to the Prime Minister and a group of interested bankers and government representatives, who approved the procedure. The test of the compensation process was conducted with the cooperation of an attorney who was responsible for the liquidation of a small bank having less than one thousand depositors.

The development of the deposit compensation program for the Bank Baltija depositors in less than one month was the significant product of a co-operative effort among the major governmental financial institutions of Latvia (the Ministry of Finance, the Bank of Latvia, and the State Savings Bank) and several donor entities (World Bank, USAID, PHARE and the IMF). Having so many people representing different agenda come together and to develop and execute a successful plan marks the overall goal of co-operative donor and client effort. The country of Latvia declined the use of loans or tax income to compensate the depositors of banks. Only funds collected from the liquidation of the assets of banks would be used to repay depositors. Given the political climate this was a very conservative move, but one which had the concerns of the tax paying populace at the fore front. Since the compensation process was commenced only in August of 1995 and was slow due to use of cash payments, only six percent of the total number of covered depositors were paid before the election. When the existing government coalition was replaced, the compensation program was terminated. The basic theories of the compensation program continued to be used in the payment of depositors of other failed institutions.

Banking Supervision

The director of banking supervision appointed in the late fall had a very progressive attitude toward supervisor training. He accelerated the supervision department's move toward the acceptance and incorporation of the recently published Basle Core-Principles of Banking Supervision, recognising the role of risk based supervision and the need for a broad based training program. The Governor of the Bank of Latvia and the director of the supervision department acknowledged the universal aspects of bank supervision. Their goal was to ensure that the supervision department and its staff would be on a par with the most sophisticated in Europe. All laws and regulations adhered to the European Union Directives and in some cases were more conservative for example in the area of capital adequacy and provisioning.

Most notable among the activities was the acceptance of more training activities involving sending supervisory staff to the US and western Europe for training. While many of the supervisors were expanding their education by attending Masters Degree programs with the local universities including the Riga Branch of the Stockholm School of Economics, the Bank of Latvia encouraged language education and other activities which would broaden the horizons of their staff and make them eligible for additional training. One of the goals of the supervision department was to develop specialists in different fields of supervision activity. In each training activity, two to five supervisors were given intense training in a field so that they could act as a resource for the other supervisors. Training more than one specialist was important since as these supervisors were trained they became attractive to the private banking industry and frequently left the Bank of Latvia for jobs in the private

In 1996, ten of the fifty members of the financial institutions supervision department attended training in the United States. With the assistance of USAID, some attended the Financial Institutions Analysis Course presented by the Federal Reserve and some attended the World Bank/Federal Reserve seminar on bank supervision in emerging markets. Many visited with financial institutions in the United States to study commercial banking practices. This activity continued in 1997 expanding to include Latvian supervisors on bank examinations with US regulators.

With the goal of "life after advice" always in mind the Barents Group resident advisors developed and expanded on a Bank Supervision Manual for the Bank of Latvia. This was a co-operative effort between the resident advisors and the supervision staff with the idea that the supervision staff would be those responsible for updating and changing the manual in the future. Other Barents training endeavours included a six week short term advisor program on white collar crime which included seminars on money laundering for supervision staff, recommendations of forms and procedures for criminal referral activities and the adoption of supervision practices for examination of suspected money laundering transactions. Barents also set up a training handbook for the supervision department detailing an outline for training and training response. These special training activities and those listed below were ancillary to the day to day opportunities for interacting with the supervision staff and others within the bank on general questions, acting as a sounding board for ideas, and responding to enquiries.

The training activities at the Bank of Latvia for bank supervisors was a co-operative effort between many USAID funded activities. During 1996 and 1997, FSVC provided four Federal Reserve examiners for specialised seminars in Foreign Exchange, Securities and Non traditional banking activities such as trusts and subsidiaries. FSVC also was able to provide a NASDAQ supervisor to discuss

securities issues with the supervisory staff and the emerging securities and exchange commission.

The USAID funded Barents Group advisor arranged for the Riga Stock Exchange to make two presentations to the bank supervision staff on the workings of the stock exchange and the mechanics of stock transactions. While this activity was not funded by USAID, it was determined by the advisor to be very effective in encouraging co-operative effort between the stock exchange and the supervisors of the Bank of Latvia and in developing skills needed for the supervision staff in evaluating bank's transactions on the Riga Stock Exchange.

The Riga Business School, another USAID funded activity, provided a train the trainer activity for the bank supervision staff which was part of an overall plan to prepare the supervision department for sustainability or "life after advisors". Each time a supervisor returned from a seminar or training activity outside of the Bank of Latvia, he or she was required to make a presentation to the rest of the staff. The goal here was to develop a sharing of information process so that individual training would serve the entire department in the long run.

The overall goal of the bank supervision support activity was to achieve a supervision department and staff that would be able to examine banks anywhere in the world, given the universality of supervision activities. As the resident advisor program drew to a close, the supervisors of the department took three examinations to attain a certification that they met "international" standards or best practice standards for supervision staff. The first test covered knowledge of Latvian banking law and regulations, the second covered general knowledge and credit evaluation and the third covered a sample bank examination. All members of the supervisory staff passed these three tests and attained certified examiner status. Each was rewarded with a certificate of completion and a pin bearing the logo of the Bank of Latvia. The pins were awarded by the Governor and the Deputy Governor of the Bank of Latvia and by the United States Ambassador to Latvia Larry Napper.

The qualifications and expertise as supervisors of the Bank of Latvia supervision staff has been further recognised by the fact that during 1998, six Bank of Latvia examiners participated in a TACIS funded project to assist in examinations with the supervision department of the National Bank of the Ukraine.

Other Activities

The Bank of Latvia was very progressive in requiring that all Latvian banks keep their records according to International Accounting Standards. However, this put the local accounting community and non-English speakers in the banking community on an unequal footing, since these standards were in only English. At the request of the Bank of Latvia and the Ministry of Finance, USAID funded a project to translate the IAS and the International Standards of Auditing. This project was developed in concert with World Bank activities related to Accounting Reform. The Bank of Latvia edited and published a Latvian translation of International Accounting Standards subsequent to the end of the resident advisor program.

Summary

After the termination of the resident advisor program, USAID continued assistance to the Bank of Latvia on an intermittent basis with assistance in the

writing of regulations and with training on treasury activities and continued training in the United States. The Bank of Latvia has continued to improve its supervision staff and refine its regulations.

Attachment

2. Ms. Kathryn Woolford: Trip Report 1/99

Memorandum to:

Lori Yerzyk

Director

Barents Group, LLC

From:

Kathryn Woolford Senior Advisor

Date:

15 January, 1999

Subject:

Strengthening Banking Supervision

Bank of Latvia Visit Report

From Monday, January 11th until Wednesday, January 13th, this advisor and Susan Ballenger visited with the Bank of Latvia and with members of the banking community to discuss issues related to supervision and treasury products and activities. Ms. Ballenger remained with the Bank of Latvia supervision staff to consult with and give lectures on these products and topics.

The Bank of Latvia Supervision Staff had requested instruction and assistance concerning "Capital Markets", this request was very broad in its range of topics for discussion and assistance and therefore the first two days of the project were spent in defining the specific targets to be addressed and the level of that address during the remainder of the period.

Ms. Ballenger and myself visited with Mr. Michael Bourke of Rietumu Bank, Mr. Karlis Grinbergs of Unibanka and with Mr. Richard Symonds of the Barents Group Capital Markets project in Riga. We also visited with Mr. Howard Handler, Mr. Bob Maushammer and Ms. Indra Arone of USAID.

Ms. Ballneger has indicated that she will review the pertinent sections of the manual to bring them up to date with the current materials on the subjects. However, this will be a task that is ancillary to the main thrust of teaching classes and working with specialists on these issues. The Bank of Latvia has specialists for target areas within the manula and they periodically update the Latvian version of the manual. There is an ongoing manual update process within the supervision department.

While in the bank in preparation for project presentation, Ms. Ballenger and myself met with Ms. Ludmila Vojevoda, Ms. Lena Lebedeva, Mr. Armands Steinbergs, Mr. Janis Placis and Mr. Janis Brazovskis. We also met with other members of the staff on an informal basis to determine the level of knowledge on treasury issues and types of instruments used by the banks. One of the drawbacks of specialization at the Bank of Latvia is that some of the individuals that we met with are not familiar with the general usage of products. However, it is hoped that Ms. Ballenger's presentations and assistance will fill that gap to some

After discussions with bankers and supervisors alike and most specifically after reviewing documents on some commercial bank transactions provided by the central bank, it was determined that this training had come at a very crucial time. The effects of the Russian crisis will clearly be shown in the Latvian banking system as the audited financial statements are published in the coming months.

One of the concerns of the Bank of Latvia which will not be addressed by Ms. Ballengers' assistance is that of accounting and disclosure for derivatives. As this is still an issue of discussion in the accounting field around the globe,

this writer recommended to Ms. Vojevoda that perhaps the bank would be able to contact the accounting advisor to the Barents Capital Markets project who is an experienced educator in this field.

Thirteen members of the Bank of Latvia supervision staff have recently spent up to three months each in the Ukraine, giving assistance in bank supervision to the National Bank of Ukraine supervision department. Ms. Vojevoda indicated that during this project, the Bank of Latvia supervisors all carried their copies of the Bank Examination Manual to use while they were giving this assistance. This indicates their respect for and use of the manual.

USAID has requested a end of contract paper to be included in their close out materials. This topic was discussed at the meeting with USAID in Riga.

Attachment

3. Ms. Susan Ballinger: Trip Report 1/99—Capital Markets Specialists

Trip Report Capital Markets Specialist Ms. Susan Ballinger January/February 1999

The consultant spent the first three days of the two-week assignment developing an understanding of the banking supervisors' familiarity with capital market products and the issues they face when examining Latvian banks engaged in those activities. Meetings to discuss training requirements were held with the senior managers of Banking Supervision—Armands Steinbergs and Janis Placis and several of the BOL staff. The consultant also visited two local banks (Unibanka and Rietumu banka), Barents/USAID capital markets project and USAID to get more perspective on the markets.

During this first week, two half-day seminars were given at the BOL for 10 examiners. The first (in English) was a case study on Long Term Capital Management—the controversial hedge fund that sustained large trading losses during the August 1998 market crash. The purpose of this case study was twofold. The first was to illustrate how even the "best and the brightest" traders and academics can fail when they exceed their defined mandate and the markets are illiquid. Second, an introductory case study/discussion early in the first week was useful for the consultant to gauge the examiners' familiarity with capital markets products and related risks.

Eight examiners also requested a seminar (with translator) on Global Depository Receipts, since the first Latvian bank (Unibanka) had recently issued receipts. The examiners had concerns as to their responsibilities for supervising such transactions and subsequent operations. Other one-on-one consultations with the BOL staff covered such topics as: disclosure report requirements; interpreting EU/Basle capital adequacy directives; accounting for futures and forwards; hedging open foreign exchange positions with options.

During the second week the consultant conducted two courses on *Treasury Risk Management* (see attach course outline) at the Bank's training center outside Riga. The first course was 3 days (6 hours/day), with simultaneous translation, for 14 examiners who had little experience with Treasury products. The second course, in English, was two days (6 hours/day) for 11 examiners who had examined banks' treasury departments.

Treasury Risk Management Course Outline

- 1) Phases of Risk Management
- 2) Treasury Risks
 - a) Definitions
 - b) Types of Hedge
 - c) Cash vs. Derivatives Markets
- 3) Foreign Exchange Transactions Terminology
 - a) Value Date Determination
 - b) Creating an FX Position
 - c) Dealer Blotter Records
- 4) Spot Foreign Exchange
- 5) Forward Foreign Exchange
 - a) Derivation of Forward Rates
 - b) Role of Spot Rate and Interest Rates
 - c) Calculating Forward Points
 - d) Premiums and Discounts
 - e) Interpolations
 - f) Calculating Profit/Loss
 - g) Exercising and Quoting Bid/Offer Rates
- 6) Foreign Exchange Swaps
 - a) Uses of Swaps
 - b) Calculating and Quote Swap Points
 - c) Short-Date Swaps
 - d) Arbitraging FX and Money Markets
 - e) Cost of Forward Cover
 - f) Exercising and Quoting Bid/Offer Rates
- 7) Netting Agreements
- 8) Futures Markets
- 9) Managing a Bank's FX Position
 - a) Position Analysis
 - b) Setting Limits
- 10) Money Markets
 - a) Product Definitions and Terminology
 - b) Day Count and Bases Calculations
 - c) Positions

Treasury Risk Management Course Outline- continued

- 11) Yield Curves
 - a) Definitions
 - b) Strategies
- 12) Liquidity Risk Management
- 13) Interest Rate Risk Management
- 14) Uses of Derivatives
- 15) Derivative Risks and Disasters
- 16) Introduction to Currency Options
 - a) Vocabulary
 - b) Puts and Calls
 - c) Options Premiums
- 17) Interest Rate Caps, Floors and Collars
- 18) Basics of Interest Rate Swaps
 - a) Definition and Market Terminology
 - b) Types of Swaps
 - c) Risks
- 19) Setting Risk Management Policies & Guidelines
- 20) Records and Reporting
- 21) Organizational Structure
- 22) Operational Risks

Attachment

4. U.S. Training Participants: Courses Attended/Internships

Barents Group LLC

Bank of Latvia U.S. Training Participants

Names	Course Participated	Date
1.) Alex Rakojeds	Financial Analysis SchoolBoard of Governors	August/September 1997
2.) Janis Placis	World Bank/Federal Reserve Bank Analysis School	October/November 1997
3.) Maris Avontins 4.) Gunta Suce	Financial Analysis School -Board of Governors	May 1998
5.) Ludmila Vojevoda	Financial Analysis SchoolBoard of Governors	July 1998
6.) Maris Graudis	Internal Controls & AuditFederal Reserve Bank of NY	July 1998
7.) Diana Vasarmane	Credit Risk AnalysisBoard of Governors	August 1998

Bank of Latvia U.S. Training Participants

Names	Course Participated	Date
8.) Edgars Diure	Internal Controls & AuditFederal Reserve Bank of Chicago	April 1998
9.) Ilze Rainska	Real Estate LendingFederal Reserve Bank of Texas	August 1998
10.) Zigrida Stabulniece 11.) Gunta Suce	Capital Markets SeminarFederal Financial Institution Examination Council	February 1999
12.) Janis Placis	Real Estate Lending SeminarFederal Reserve Bank Texas	March 1999

^{***}For Course Descriptions refer to Federal Reserve System Training Program Course Catalogue 1998 or 1999****

BRACEWELL & PATTERSON, L.L.P. A REGISTERED LIMITED LIABILITY PARTNERSHIP ATTORNEYS AT LAW

SOUTH TOWER PENNZOIL PLACE
711 LOUISIANA ST STE 2900
HOUSTON TX 77002-2781
713 223 2900

713 223 2900 FAX 713 221 1212

ROBERT L. CLARKE

August 18, 1998

100 CONGRESS AVE STE 1900 AUSTIN TX 78701-4052 512 472 7800

LINCOLN PLAZA 500 N AKARD ST STE 4000 DALLAS TX 75201-3387 214 740 4000

2000 K STREET NW STE 500 WASHINGTON DC 20006-1872 202 828 5800

43 BROOK ST LONDON WIY 2BL ENGLAND 44 71 355 3330

Mr. Ludmila Vojevoda
Head of Methodological Division
Credit Institutions Supervision Department
Latvijas Banka
K. Valdemara Iela 2A
LV 1050 Riga
LATVIA

Re: Supervisory Agreement of Cooperation

Dear Ludmila:

I have finally been able to put my hands on a copy of the Statement of Cooperation that I mentioned on my last trip to Latvia. This one is among the Office of the Comptroller of the Currency, the Federal Reserve System and the Superintendent of Banking in Chile. I believe it provides a good model to use in entering into similar arrangements between the National Bank of Latvia and other international supervisors.

Please let me know if you have any questions about the document or need any additional information in that respect.

Very truly yours,

Bracewell & Patterson, L.L.P.

Robert L. Clarke

my imme

RLC/gc Enclosure

cc: Ms. Lori Yerzyk

Barents Group, LLC

50.30A9 14:58

Board of Governors of the Federal Reserve System

Superintendencia de Bancos e Instituciones Financieras

Office of the Comptroller of the Currency

STATEMENT OF COOPERATION

In view of the fact that a number of banking organizations chartered in the United States and Chile have operations in each of the respective jurisdictions, the Board of Governors of the Federal Reserve System (the "Board"), the Office of the Comptroller of the Currency (the "OCC") and the Superintendencia de Bancos e Instituciones Financieras de Chile (the "Superintendencia") have reached an understanding in order to establish an arrangement for the sharing of supervisory information to facilitate the performance of their respective duties and to promote the safe and sound functioning of financial institutions in their respective countries. This understanding also demonstrates the commitment of the Board, the OCC and the Superintendencia to the principles of consolidated comprehensive supervision and cooperation among banking regulators.

The Board, the OCC and the Superintendencia express, through this understanding, their willingness to cooperate with each other on the basis of mutual trust and understanding in the

supervision of cross-border branches and other establishments of banking organizations incorporated in the United States and Chile.

Sharing of Information

The Board, the OCC and the Superintendencia recognize that close communications between home and host supervisors would be mutually advantageous. Cooperation would include contact during the authorization process (including both issuance and revocation of any branch license) as well as in the supervision of the ongoing activities of such entities. Consequently, the three agencies intend to:

1. notify the appropriate home supervisor(s), without delay, of applications for approval to establish offices in one country by banking organizations from the other country. In addition, upon request, the home supervisor(s) would inform the host supervisor(s) whether the applicant bank is in substantial compliance with banking laws and regulations and whether the bank may be expected, given its administrative structure and internal controls, to manage the branch or other cross-border establishment in an orderly manner. Furthermore, to the extent reasonable and consistent with law, the supervisors would share information that may reflect adversely on the capability, integrity, or experience of the prospective managers of the cross-border establishment.

65:41 86 62 Ade

- 3 -

- 2. endeavor to notify the appropriate home supervisor(s) and provide relevant information regarding any material developments or supervisory concerns in respect of the local operations of any banking organization headquartered in the other country.
- 3. respond to requests for information on any aspect of their respective national regulatory systems and inform each other about any major changes, in particular about those which have a significant bearing on the activities of cross-border branch and other establishments by banking organizations incorporated in the respective other country.
- 4. endeavor to inform the appropriate host supervisor(s), in a timely manner and to the extent reasonable, about any event which has the potential to endanger the stability of banking organizations with cross-border establishments in the respective other country. They would also inform the appropriate supervisor(s) in the other country of administrative penalties imposed, or any other formal enforcement action taken, on a cross-border establishment as host supervisor or on the banking organization as home supervisor if they judged the information as possibly important to the supervisors of the other country as it may relate to the operation of the cross-border establishment.

98 14:59 PPR 14:59

- 4 -

Whenever appropriate, ad-hoc meetings would be arranged to resolve serious supervisory problems concerning a cross-border establishment.

Supervisory Cooperation

- 1. The Superintendencia, the Board, and the OCC agree that cooperation is particularly useful in assisting each other in carrying out on-site inspections of cross-border establishments in the host country. The home supervisors would inform the host supervisors of both the commencement and conclusion of the audit or examination of the cross-border establishment in the host country and provide information on the results of the review to the extent reasonable. Consultation and cooperation may include sharing information as may be reasonable on the results of audits or examinations of banking organizations relevant to the operations of the cross-border establishment.
- 2. The agencies also would conduct meetings as often as appropriate to discuss issues concerning banking organizations which maintain cross-border establishments in the respective other country.

General Provisions

1. Information would be shared to the extent reasonable and subject to any relevant statutory provisions, including those

restricting disclosure. In addition, the provision of, or request for, information under this understanding may be denied on grounds of public interest or national security or when disclosure would interfere with an ongoing investigation.

- 2. To the extent permitted by law, each agency would hold confidential all information (other than publicly available information) received from the other pursuant to this understanding.
 - 3. This Statement supersedes the Statement of Cooperation between the Board and the Superintendencia that became effective on March 10, 1997.

The Board, the OCC and the Superintendencia may promote their cooperation through visits for informational purposes and by exchange of staff for practical internships. In addition, the Board, the OCC and the Superintendencia would pursue areas where the training of staff at either agency would benefit from input and support by the other agency in order to reinforce sound banking supervisory practices in both countries.

- 6 -

The Board, the OCC and the Superintendencia look forward to continued cooperation and discussions on these and other supervisory matters.

Confirmed:

Board of Governors of the Federal Reserve System

Richard Spillenkothen Director

Division of Banking Supervision & Regulation Superintendencia de Bancos e Instituciones Financieras

By . José Florencio Guzmán Superintendente Superintendencia de Bancos e Instituciones Financieras

Office of the Comptroller Of the Currency

Susan F. Krause

Senior Deputy Comptroller International Affairs

Dated:____



MAY 2 U 1998

DATE-	Riga, May 19, 1998	
TO-	Mr. Horward R. Handler, Co	ountry Representative USAID, Riga, Latvia
FAX.	783 0067	
PHONE.	732 5494	OPTIONAL FORM 99 (7-90)
FROM- FAX- PHONE-	Bank of Latvia + 371 702 2420 + 371 702 2300	To LOVI YETEIK Dept.//Agency Exercise To Dept./
PAGES- SUBJECT-	I, including this cover page Mr. Bob Clark visit	102) 463 6669 101 (371) 6500 67 NSN 7540-01-017-7368 5088 101 GENERAL SERVICE ADMINISTRATION

Our ref.: 08 - 13/944

Dear Mr. Handler,

On behalf of the Bank of Latvia we would like to express our gratitude to the U.S. Agency for International Development for your efforts in strengthening the relationship between the Bank of Latvia and the specialists of the Barents Group.

As of this writing, we at the Bank of Latvia are working on a draft of the regulation "On Consolidated Supervision". As you know, this area is of vital concern to the Bank of Latvia and important from a supervisory standpoint.

With this in view, we would kindly ask the U.S. Agency for International Development to consider the possibility of arranging Mr. Bob Clark's visit to the Bank of Latvia, during the week of June 1, 1998, to discuss this matter and to assist us in further work on the regulation. We feel that Mr. Clark's expertise would be of invaluable help to us.

Yours sincerely,

limais Rimšēvičs

Chairman of the Executive Board

Bank of Latvia

Armands Šteinbergs

lead of the Credit Institutions
Supervision Department

Bank of Latvia

FAKSS

LATVLIASBANKA • K. VALDEM RAIBLA 2A • LV-1060 R.GA • LATVLIA • T. LPLNIS +371 702 2500 • FAKSS +371 702 2420 • TITLEKSS 161146 EN. KLV

6. International Accounting Standards-Publication—Press Release



iarone@usaid.gov on 10/21/98 10:09:54 PM

To: katewolf@starnets.ro, Lori Yerzyk/fininst/Barents

cc:

Subject: Looking to past ...

Hi, Kathryn and Lory,

The BOL finally issued IAS 1997 (with 2 amended IAS, as I understood)! It took long to finalize everything. Ms. Pilsuma told me that there are 2000 copies. Publisher and wholesaler is "Jana Seta". Wholesale price - about 20 lats.

You (Kate) may remember the BOL's newspaper (A3format) "Averss un Reverss" (only in Latvian). Its latest issue no.5, 1998 contains Ms. Pilsuma's article on this event. Besides general info on IASC, IAS etc. it gives also whole long list of institutions and persons they thank. USAID and KPMG/Barents group also is mentioned as initiators of a process.

It means that you -ladies- also should be thanked for this idea. It was breaksthough in one point. Many events have happened after that (good and not so good) - process has continued. In state level - nothing has been decided how to make standard setting process work and get them actually implemented, but at least now professionals without english knowledge can start to be more informed, involved etc. We pay big attention to changing an adoption procedure within our new capital markets project.

Regards, Indra

7. Miscellaneous News Clippings (1st Quarter 1999)

Latvian banks seen weathering collapse of Rigas Komercbanka

Central bank says EBRD failed to convey pertinent methods to sustain a recovery

atvia's bank system can survive the collapse of fifth-largest Rigas Komercbanka (RKB), closed by the central bank during March 6-7, but the episode could damage the sector's credibility, analysts said on March 8. They also said the credibility of the European Bank for Reconstruction and Development (EBRD) — RKB's single largest shareholder with at 23.07 percent — would also be hurt.

By Martinsh Gravitis

The central bank earlier said the EBRD had done too little to impart prudent risk management practices on RKB and had not adequately aided in its recovery. The EBRD said earlier last Monday it would stick with RKB for the long haul and urged officials to come up with a scheme to resuscitate the institution.

Prime Minister Vilis Krishtopans said RKB's collapse would not pose a systemic threat to Latvia's bank sector - which suffered a severe crisis in 1995 after the country's largest bank, Banka Baltija, went under. "The Latvian banking system is stable and secure, it has weathered tremors (in the past)," Krishtopans told a news conference. He also stood by the action of the central bank, which said other banks had not been as heavily exposed to Russia as RKB. "The strict stance of the Latvian central bank will increase trust in the Latvian banking system and the economy as a whole," Krishtopans said.

No other choice but to shut down

Analysts have agreed, saying RKB's dire straits gave the central bank little choice but to shut it down. The central bank said Komercbanka's losses not backed by equity amounted to could be as high as 30 million lats due to its risky Russian investments.

The bank lost some 73 million lats since late August - when it endured a three-day run on deposits - and 27.5 percent of its assets had been frozen in accounts with Russian financial institutions as a result of the financial turmoil there.

"I think acting with such determination is clearly good and it underlines that much has been learned from the collapse of Baltija," said independent Baltic strategist James Oates. However, Oates said Komercbanka's failure reflected poorly on the EBRD, whose presence is usually seen as reassuring. "One thing is clear is that the supervision of the EBRD has been inadequate," Oates said.

Struggling rescue plan likely

Despite the EBRD's determination to stick with RKB, analysts said the institution's huge losses would probably make any

rescue plan a difficult one to sell on any investor. They also said the episode would damage the credibility of Latvian capital markets due to earlier reports by RKB that played down the extent of the damage done to it by Russia, although the market had not believed these.

"It was clear to everyone else that the loss was much bigger.... I didn't like how this was being handled from the very beginning," said Hansabank Markets broker Girts Ozols. RKB in earlier said its 1998 loss - based on unaudited figures - was 1.2 million lats, although it said it was reevaluating its securities portfolio with auditors.

"Komercbanka reporting an 1.2 million lats unaudited loss for 1998 in January was a clear case of (giving) misleading (information), but otherwise earlier exposure figures enabled people judge independently," said Roberts Idelsons, head of securities at Trasta Bank. (Reuters)

Latvia votes for Europe

RIGA

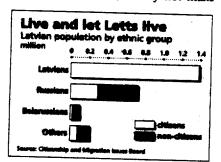
HEN Latvians went to the polls on October 3rd, they were doing more than electing a new parliament and answering a referendum question on the liberalisation of citizenship laws. At stake was Latvia's bid to join the European Union and thereby to yoke itself ever more firmly to western and northern Europe, in its continuing effort to be rid of its Russian connections.

Latvia would dearly love to join its neighbour, Estonia, on the fast track to membership of the EU. But even if the EU would have it, Latvia would find it hard to shake off its Russian ties altogether. For one thing, seven years after it pulled itself free of the Soviet Union, over 700,000 ethnic Russians still live there. Although many of them have been there since Soviet times, three-fifths of them do not have Latvian citizenship. Russia says they and their children should be granted it automatically, but Latvia has so far steadfastly refused to give it to them, requiring everyone to pass a Latvian language and "culture" exam before getting citizenship.

The row between the two countries, chiefly over this issue, became particularly vicious earlier this year. Yuri Luzh-

kov, Moscow's populist mayor, compared the Baltic state to Pol Pot's Cambodia. President Boris Yeltsin threatened economic sanctions. EU governments have made it plain that they simply want the matter settled, and Latvia to get Russia, which is determined to retain its clout in its former colony, off its back.

Hence, in part, the referendum. On the day, 53% of Latvians backed the revised citizenship proposal, enough to make it law. Supposedly, this will speed up the naturalisation of ethnic Russians: it opens up applications to all residents, and gives citizenship automatically to children born in the country since 1991. In practice, however, it may not make



much difference. The Baltic Russians are a disaffected bunch. Few of those who qualified for citizenship even under the old law actually applied for naturalisation. Most Russian-speakers fear they will fail the language and culture exam, which remains in place under the new law. Besides, why apply for a Latvian passport when Russia charges hefty visa fees to Latvian citizens, and young men have to do military service?

Whether or not Latvia manages to settle its differences with Russia, the outcome of the election confirms the country's westward yearnings. Two solidly pro-European parties came out on top. The People's Party, led by Andris Skele, a former prime minister, is now hoping to patch together a coalition with Latvia's Way, whose platform—including support for a stable currency and the privatisation of the few firms that remain in state hands—is virtually identical to its own. But the two parties are bitterly divided over who would lead the government.

Together, the two parties have only 45 seats in the 100-seat parliament. To build a majority, they will probably look either to Fatherland and Freedom, the outgoing right-wing nationalist party, which is vehemently opposed to the liberalisation of citizenship laws, or the centrist New Party, led by Raimunds Pauls, a musician.

THE ECONOMIST OCTOBER 10TH 1998

_				
_	 -	_	242	_
	н	-	ш	и.

Article 21 of 745

ESTONIA'S OUTGOING MINISTER URGES NEW GOVT TO SIGN THREE ACCORDS WITH RUSSIA

03/23/99

Baltic News Service

Copyright(C) 1999 Baltic News Service, Source: World Reporter (TM)

TALLINN, Mar 23, BNS - The outgoing Estonian Roads and Communications Minister Raivo Vare said it is important to sign three important agreements with Russia before this fall's Russian general elections, which could lead to worsening of relations between the two countries.

Vare, who is head of a group of economic talks between Estonia and Russia, said that agreements on most-favored nation status, avoidance of double taxation and the mutual protection of investments should be signed soon. Signing of the accord on most-favored nation status would mean elimination of the present double customs duties.

The outgoing minister said that delay with the signing of the agreements would postpone them indefinately, because the political climate in Russia will likely become colder after the elections.

Unfortunately, foreign investments into Estonia are directly connected with Russia and Estonia's relations with its neighbor, Vare told reporters on Tuesday. "Foreign investors see Estonia above all in the Russian context," he said.

"All this must take place before the fall," said Vare, adding that on specialists' level agreement has already been reached. He said that in substance, the agreements in question are typical, and the presumption of their signing is political consensus.

The next meeting which should take us a step closer to the signing of the three important agreements will take place on April 6, Vare said.

(et a n to deadlines)

Copyright © 1999 Dow Jones & Company, Inc. All Rights Reserved.

44

Central banks always take a risk when they close down a bank, but it is also true that decisive action is sometimes better for a banking system than no action at all.

Meanwhile, the Bank of Latvia can be reassured by the fact that banking crises do not only happen in Latvia. Listening to the radio at the weekend, I was intrigued to hear the following story that has a clear echo in Latvia.

The Indonesian government, it was reported, has decided to close 38 banks, take over seven others and inject capital into nine more at a cost of \$35 billion. Sorting out the banking sector is widely seen as the key to economic recovery in Indonesia and there is no reason why the same logic should not apply to Latvia, albeit on a much smaller scale.

Only time will tell what will eventually be salvaged from Komercbanka, but I would not be at all surprised if, in the final analysis, the Bank of Latvia has once again proved itself to be a shrewd operator in a difficult and volatile market.

Chris Butler is a Senior Manager with Pricewaterhouse Coopers in Vilnius. If you have any questions or comments he can be contacted via TBT in Vilnius.

Retain to Headlines

Copyright © 1999 Dow Jones & Company, Inc. All Rights Reserved.

 - 44	ITIC

Article 7 of 745

Business

Nipping a new crisis in the bud

03/18/99

The Baltic Times

Copyright (C) 1999 Baltic Times; Source: World Reporter (TM)

There was a nasty sense of deja vu about the news from Latvia last week that the central bank had stepped in to close Rigas Komercbanka. When I first arrived in the Baltics in 1995, the biggest news was of collapsing Latvian banks.

The largest of them, Banka Baltija, remains in the headlines to this day due to the size of its losses and the numbers of private citizens who lost money in it.

Four years later it seems as though nothing much has changed. RKB, like Banka Baltija, is a bank with large numbers of private and commercial customers throughout Latvia.

RKB, also like Banka Baltija, seems from the public pronouncements coming out of the Bank of Latvia to have been the victim of events in Russia rather than anything closer to home.

Scratch the surface, however, and it becomes evident that plenty is different between these two cases, and plenty has changed.

The Latvian banking sector is, for a start, much better regulated than it was in 1995.

Stricter requirements are in place covering, for example, accounting, financial reporting, auditing, capital adequacy and even fitness to be a bank shareholder in the first place.

While there was more than a whiff of scandal about the death of Banka Baltija, so far it seems that this is not likely to be the case with Komercbanka.

It could very well be that the closure of Komercbanka is an example of a bank that simply got into trouble due to business decisions, taken in good faith, that with the benefit of 20/20 hindsight turned out to be bad ones.

In other words, it is quite possible that when the history books are written, Komerchanka will be seen to have been a business casualty. In a strange way, this is progress.

It is still early days of course, and the fate of the bank is far from sealed.

Indeed, there has been criticism leveled at the Bank of Latvia, not least from Teodors Tverijons, head of the Latvian Commercial Banks Associations, for having taken precipitate action.

As he put it, the 1995 banking crisis took away people's confidence for a long time.

By 1998 confidence had largely returned, but the closure of Komercbanka represents another huge step backwards and in his opinion has probably put an end to any attempts to re-finance the bank.

Certainly, it is true that confidence is the fuel of the banking business and it is always a cause for concern when something happens to reduce that confidence.

41,

_				
	_	_	142	_
	-	•	Iti	•

Article 9 of 709

Latvian banks' 1998 losses considerably exceed pre-audit figures

03/23/99

BBC Worldwide Monitoring

Source: ETA news agency, Tallinn, in English 1711 gmt 21 Mar 99/BBC Worldwide Monitoring/(c)

BBC

Text of report in English by Estonian news agency ETA on 21st March

[No dateline as received] The total losses of the eight Latvian commercial banks that have released their audit reports, already amount to 40.673m [lats]. This is far more than the pre-audited losses of all commercial banks of Latvia, which totalled 28.896m lats.

Unibanka's audited losses totalled 15.07m [lats] in 1998, which is up from the 8.7m [lats] of pre-audited figures. Rietumu Banka's [Western Bank] audited losses stood at 12.213m [lats] last year, up from 7.139[m lats] of pre-audited lasses. Baltijas Tranzitbanka's (Baltie Transit Bank) audited losses were 6.165m lats; the bank had earlier posted 3.247[m lats] in pre-audited losses. Hansabank-Latvia posted 3.2m lats in audited losses, and 2.985m [lats] in pre-audited losses. Saules Banka's [Sun Bank] audited losses in 1998 totalled 1.935m lats, up from 1.524m in pre-audited losses. Multibanka's audited losses were 1.589m lats in 1998. The bank had posted 1.586[m] lats in pre-audited losses. Latvijas Investiciju Banka's (Latvian Investment Bank) audited losses totalled 667,000 lats last year, up from 523,500 lats in pre-audited losses. Latvijas Tirdzniecibas Banka (Latvian Trade Bank) is so far the only bank that posted profit last year. The bank's audited profit was 166,000 lats in 1998, the bank had earlier posted 172,000 lats in pre-audited profit.

Retain to deadlines.

Copyright © 1999 Dow Jones & Company, Inc. All Rights Reserved.

8. Letters of Appreciation from Latvian staff to USAID/Barents Group LLC

Barents Group LLC



mihaelab@starnets.ro on 09/02/98 09:28:27 AM_

To:

Lori Yerzyk/fininst/Barents

CC:

Subject: Trip to USA

Information on the trip to the states from Daina Vasermane. Seems like she enjoyed herself. I would be interested in hearing how the FDIC crew received her. Her response was so different from the Romania people.

kat

<---- Begin Forwarded Message ---->

From: Daina Vasermane <Daina_V@bank.lv>

To: "'mihaelab@starnets.ro' " <mihaelab@starnets.ro>

Subject: Trip to USA

Date: Wed, 2 Sep 1998 15:18:05 +0300

Dear Kathryn,

I just want to thank you for the great opportunity I was given. It was really great to travel to Washington, DC, where I could meet all my family. But still more exciting it was to travel to Florida. I have never been so far to the South in any place of the world. I saw the palm trees and the green ocean for the first time in my life. I've met very nice people there and had a great time while examining the bank. Everything went on quite well, and I am back in my office at last. Everything seems now as if a very nice dream.

Best wishes and kind regards, Daina

<---- End Forwarded Message ---->

Lori Yerzyk/fininst/Barents

<---- End Forwarded Message ---->

To:

mihaelab@starnets.ro on 01/29/99 07:25:14 AM

Subject: FW: Would you please forward this to Susan Ballinger. I have lost her email address. <---- Begin Forwarded Message ----> From: Tamara Drozdova <Tamara@bank.lv> To: "'mihaelab@starnets.ro'" <mihaelab@starnets.ro> Subject: FW: Date: Fri, 29 Jan 1999 14:17:20 +0200 > ----Original Message----> From: Tamara Drozdova > Sent: Friday, January 29, 1999 1:57 PM > To: 'michaelab@starnets.ro' > Subject: > Hello! > How are you? > I was going to write you all this week, but you know how it is > I want to say you that we enjoyed Susan's lectures very much. It was > exactly what we needed. We were divided into two groups. One group worked > with translator, other - without. > I hope she enjoyed her being in Riga, too. > At last real winter came in Riga: -17, snowing. Even sun is shining today! > It seems to me first time this year. > Have a nice weekend and don't disappear. > Tamara

Tamara Drozdova <Tamara@bank.lv> on 02/11/99 08:09:59 AM

To: Lori Yerzyk/fininst/Barents

cc:

Subject: RE: FW: Susan Ballinger

Dear Lori

It was very nice to hear from you. We really enjoyed Susan's visit. She is very nice person and very professional.

I think for everybody in BoL, who somehow was involved in Barents group project, this cooperation was very useful. We met so many nice people! I hope, too, to be in contact with you. Now I leave between Latvia and US because of my husband, who works in Atlanta. Last year I was twice in US and nobody knows what will be the end of this story, maybe I call you some days from WDC?

Best wishes and good luck in your new projects!

Tamara

----Original Message----

From: lyerzyk@barents.com [mailto:lyerzyk@barents.com]

Sent: Wednesday, February 10, 1999 6:28 PM To: mihaelab@starnets.ro; tamara@bank.lv

Subject: Re: FW: Susan Ballinger

Tamara- I was happy to hear that you were pleased with Susan Ballinger's visit. She is very knowledgeable. It looks like our contract will be ending in March. I however, plan to remain in touch with you and the others and also will always look forward to hearing from all of you.

Stay warm in the cold Latvia winter! Lori



Riga, August 28, 1997

Our ref.: 11 - 06.7.2/13

Ms. Lori Bittner Yerzyk
Manager, Financial Sector Regulatory Practice
Barents Group LLC
2001 M Street N.W., Washington DC 20036
USA

Technical Assistance to the Bank of Latvia

Dear Ms. Jerzyk,

With reference to your letter of August 1, we would like to express our gratitude to Barents Group for the assistance provided to the Credit Institutions' Supervision Department of the Bank of Latvia. We highly appreciate the previous contribution of Barents Group in developing banking supervision in Latvia and, especially, the counsel of Ms. Kathryn Woolford, and were pleased to learn about the new opportunities of cooperation between Barents Group and our bank, with the support of US AID.

We are pleased to inform you that we have already received the shipment of the reference library for the Supervision Department that will be of a significant assistance to us.

We also welcome the intention to extend the training program for the supervision staff which was initiated during the stay of Ms. Woolford at the Bank of Latvia. It would be a valuable experience for our employees to get acquainted with the practices and approaches used by the US institutions that engage in similar activities.

Also, we favor the proposition to designate a senior policy advisor who could be available to counsel the Bank of Latvia if a necessity arises. Such arrangement seems flexible enough to respond to our needs for advice in the supervision area.

Once more we would like to stress that we highly appreciate the assistance rendered by Barents Group, and look forward to our cooperation in future.

Yours sincerely,

Umārs Rimševičs Deputy Governor

Bank of Latvia

Guntis Valujevs

Head of Foreign Relations Department Coordinator of Technical Assistance

9. Latvia's Assistance to the Bank of Ukraine

10. Resident Advisor 1997 Final Report Excerpts dated July 25, 1997



Mexi

San S

July 25, 1997

Ms. Jean Lange Senior Financial Advisor USAID Washington, D.C. 20523-0039

RE: Bank of Latvia: Strengthening Bank Supervision, Phase II Contract #EPE-0005-I-00-5048-00- Task Order #5

Final Report for Resident Advisor - June 1997

Dear Jean:

Ms. Kathryn Woolford's final report is enclosed for your review. Advisor Woolford completed her tasks as a resident advisor as of month end June 1997. Ms. Woolford arrived in-country mid 1995 to assist with the banking crisis. She initially took on responsibilities for assisting the Bank of Latvia (BOL) in the resolution of a large problem bank. A second advisor was also in-country from late 1994 through year end 1995. His primary role was to provide technical assistance in the area of onsite bank supervision.

With the departure of the onsite supervision advisor, Ms. Woolford took on both roles. During her tenure, she provided technical assistance to the BOL bank suprvision department and substantial progress was made. As examples, Ms. Woolford provided guidance to the BOL in developing and implementing systems:

- to address the severe troubles in the financial sector and to implement proactive measures to minimize potential future crisis;
- to enable the examiners to supervise banks both onsite and offsite using risk management techniques;
- to train and certify examiners; and
- to comprehensively and consistently supervise financial institutions with the use of an examination procedures manual.

BARENTS

Ms. Jean Lange Page 2

)

In addition, Ms. Woolford worked with the BOL, other local government agencies and international donor organizations to coordinate the translation of the International Accounting Standards and Standards of Auditing in to Latvian.

Ms. Woolford's accomplishments contributed positively to the strengthening of the financial markets and the bank supervision department. As a result of her efforts, all Tangible Results and Benchmarks were achieved. The activities relating to each Result are addressed in this report and previously submitted monthly and quarterly reports.

Given the progress made and the commitment of the bank supervision department, a recommendation to provide ongoing periodic technical assistance to the supervision department was discussed with USAID. A modification is currently being considered by USAID and a proposal has been developed outlining specific tasks to be accomplished during an extension. The proposed ongoing assistance will provide advanced training to supervision staff and assist the BOL in developing a reference library for the examination staff. In addition, the modification will allow for short term visits to Latvia by a senior policy advisor or training experts. These visits will help to ensure that the supervisory culture is further developed and that ongoing enhancements to further strengthen the bank supervision process are achieved.

We look forward to the possibility of providing additional assistance to the Bank of Latvia through USAID. We appreciate the support and confidence of USAID- Riga and DC while working in Latvia and the strong rapport with the National Bank of Latvia. We believe that the use of short term advisors and the revised focus of technical assistance to advanced training will benefit the Bank of Latvia and help to ensure all of the technical assistance and guidance provided to date is fully understood and used to the fullest extent possible by the BOL.

If you have any questions regarding this project or have not received any of the previously submitted monthly or quarterly reports please contact me at (202) 331 - 4549.

Very truly yours,

Barents Group, LLC

Lori Bittner Yerzyk

Jon B. Herryh

Financial Sector Regulatory Practice

Manager

BARENTS

Ms. Jean Lange Page 3

cc: Mr. Howard Handler, USAID-Riga, Latvia
USAID Directorate for Policy (2 copies)
World Bank Operations Officer - Latvia
Mr. Alex Flemming
Senior Policy Advisor - Mr. Robert Clarke
Advisor - Woolford
Project File

ATTACHMENT 1

Beyond Strengthening Bank Supervision

Memorandum to:

Lori Yerzyk

Project Manager Barents Group, LLC

From:

Kathryn Woolford Kethoy Woolford

Advisor

Bank of Latvia

Date:

29 May, 1997

Subject:

Beyond the Resident Advisor Program

Strengthening Bank Supervision and the Financial System

One of the tangible results of the above referenced project is that the "bank supervision authority will have developed a training program for inspectors which leads to certification." As you know, the training program has been a success and the examiners all tested and were certified here at the Bank of Latvia. However, the training program used to train these examiners utilized several short term advisors whose specialties ranged from accounting to white collar crime. This kind of training program using outside specialists will not be repeated, mainly because the examiners are now trained and certified based on their needs and the needs of the financial system and existing regulatory frame work. In the future, the bank staff will continue to send its examiners outside of the country of Latvia to train. While the existing program set down guidelines on training needs for Latvian bank supervisors, there is no one set source for a consistent training program which will meet all of their needs.

Also, members of the banking community are reaching out for additional training, through the umbrella of the Latvian Banking Academy.

While the resident advisor segment of the Strengthening Bank Supervision project is soon coming to an end, there is a need to gradually part from the activity and create a potentially self sustaining program which will continue to insure the future strength of bank supervision and the banking community as a whole.

Not until 1996, did the Bank of Latvia's Credit Institutions supervision staff avail itself of the PIET program and courses provided by the Federal Reserve. This training experience outside of Latvia had tremendous impact on the existing project and the strength and character of the supervision department. For a small banking staff there is a very relevant need for training outside of the local supervision environment. It is also important that senior staff members be encouraged and empowered to enter into an existing structured educational program aimed specifically at bankers and individuals in activities.

Therefore, in addition to short time consultative work with senior management of the Bank of Latvia to take the role of transitioning the bank from the assistance of a resident advisor, I recommend the following three phase training program which would meet much of the future

training needs of both the Bank of Latvia supervisors and the senior management of the Latvian banking community as well. These three phases may be used in concert or separately but will enhance the work already done with the bank supervisors and strengthen the financial system through increasing the knowledge base of the Latvian Commercial bankers. Furthermore, this is a program which could be based in Latvia and expanded to meet the needs of supervisors and commercial bankers throughout Central and Eastern Europe.

I recommend using the Dallas area for some of these phases mainly because Dallas is officially the sister city of Riga and coincidentally one of six existing graduate schools of banking is located in Dallas.

Phase I Internship Program

An internship program would give both bank supervisors and commercial bankers an opportunity to work within operating entities with goals and activities similar to theirs in a western environment. There are existing internship programs with most of the regulatory agencies and major commercial banks throughout the United States. The cost of this program would be the cost of the lodging while the participants were in the United States. To be effective internships should cover at least one month of practical experience. While either the participants or their organizations could cover the cost of travel to and from the United States, it would be prohibitive to individuals coming from a country where the average salary is less than \$500 a month to cover the cost of lodging for a month. Other expenses would be the cost of coordinating the activity, that is to set up the internship engagement and to be on hand to assist the participant.

Phase II Latvian Banking Academy Graduate School of Banking Program

The Latvian Banking Academy is a complimentary activity of the Bank of Latvia. It has been supported an encouraged by the Bank of Latvia, since the Banking Academy supports the bank's goal of a strong financial system through education. It is instrumental in providing a professional certification program based on the bankers certification in the UK. Its students are members of the banking community from all levels. The Latvian banking system as well as those of Latvia's neighbors really started from scratch in the early 1990s'. The Latvian Banking Academy has worked with the Fulbright program and USIS to successfully bring the level of banking knowledge up to date. But, the Latvian Banking Academy acknowledges that there is a great wealth of knowledge on banking practices to be had in the United States banking community. It would be far more cost effective to bring an existing course of instruction to Latvia in terms of the number of participants reached.

The cost of this program would be the cost of transporting and lodging professors to Latvia to teach a concentrated course of study as it is done in the United States. The initial program would only be 10 days long, while a graduate program of study with independent study classes would compliment the concentrated course. The intent would be to develop this program, charge fees for attendance, as is done in the United States and use this fee generating capability to perpetuate the program.

Phase III Graduate Banking School and internship combination.

In courses of study such as the one described in Phase II, participants from outside the United States banking community frequently attend the concentrated course and then subsequent to that serve and internship in a local bank near the study site to reinforce materials learned during the seminar. Therefore, the recommendation is that subsequent to the first years course of study which would be held either in Riga or in Dallas, the student would then take the second years course of study in Dallas and participate in the internship program.

The cost of this would be the tuition cost for the second year of the course and the cost of lodging and subsistence and coordination for the internship program.

Summary

Developing a relationship with a particular school is not uncommon in the USAID environment, for example, here in Riga, the Riga Business School which is a masters degree program works closely with the State University of New York at Buffalo.

All three programs could stand alone or be used in concert with one another. The concept of bringing the professors to Latvia and advertising the program to a wide base of participants could have the potential to create a self perpetuating program which would live long after the close of the AID project in Latvia. Also, bringing the program to Latvia would also give the course participants a local base for assistance in the self study portion of the program. While all of the participants would speak English, there are many subtle nuances in American legal and financial terminology which might require interpretation. The Latvian Banking Academy is the logical place for this base to be set.

Since the Credit Institution Department of the Bank of Latvia is represented at the Banking Academy in the form of both students and instructors, the recommended programs would benefit the financial system from both the commercial and regulatory sides and such an organized education program would be a natural extension of the existing project.

11. Project Administration: Task Order Data (included for USAID internal purposes only)

Task Order Data

Total Level of Effort

489

Total Estimated Costs

\$781,354

a) Cumulative Level of Effort utilized as of 3/31/99:

488 days or 100%

b) Unused Level of Effort as of 3/31/99:

0 days

c) Cumulative Expenditures estimated as of 3/31/99:

\$725,000 or 93%

d) Remaining Unexpended Funds as of 3/31/99:

\$56,354

[Note: information provided above are estimates. Actual days and amounts may vary slightly once the Task Order is reconciled internally by Barents Group LLC. A final accounting/invoice will be submitted to USAID which will reflect actual days and dollars utilized during the term of this project.]

5. Mr. Robert Clarke, Senior Policy/Legal Advisors—"Statement of Cooperation" 9/98

BRACEWELL & PATTERSON, L.L.P. A REGISTERED LIMITED LIABILITY PARTNERSHIP

ATTORNEYS AT LAW

SOUTH TOWER PENNZOIL PLACE 7H LOUISIANA ST STE 2900 HOUSTON TX 77002-2781 713 223 2900

FAX 713 221 1212

ROBERT L CLARKE PARTNER

September 11, 1998

100 CONGRESS AVE STE 1900 AUSTIN TX 78701-4052 512 472 7800

LINCOLN PLAZA 500 N AKARD ST STE 4000 DALLAS TX 75201-3387 214 740 4000

2000 K STREET NW STE 500 WASHINGTON DC 20006-1872 202 828 5800

43 BROOK ST LONDON WIY 2BL ENGLAND 44 71 355 3330

Mr. Ludmila Vojevoda Head of Banking Regulations Division Credit Institutions Supervision Department Latvijas Banka K. Valdemara Iela 2A LV 1050 Riga LATVIA

Dear Ludmila:

Thank you for your recent letter. I am pleased that the Statement of Cooperation was helpful.

As you proceed with the consolidated supervision project, please let me know if there is any way I can be helpful.

Very truly yours,

Bracewell & Patterson, L.L.P.

Ino come

Robert L. Clarke

RLC/gc

Ms. Lori Yerzyk cc: Barents Group, LLC



Riga, September 7, 1998 DATE-

Mr. Robert L. Clarke TO-

partner

Bracewell & Patterson, L.L.P.

Houston TX, U.S.A.

713 221 1212 FAX-713 223 2900 PHONE-

Bank of Latvia FROM. + 371 702 2420 FAX. + 371 702 2300 PHONE.

1. including this cover page PAGES.

Supervisory Agreement of Cooperation SUBJECT-

Our ref.: 08.1-27/45 \$5

Dear Mr. Clarke.

Thank you very much for the copy of the Statement of Cooperation you mailed us. Currently the Bank of Latvia is in the process of drafting the similar agreement with the Bank of Estonia and the received document is really a good model for us to take into account.

I would like also to inform you that we are proceeding with the consolidated supervision issues and we appreciate very much the advice and comments made by you during the visit to the Bank of Latvia.

Yours sincerely,

knila Vojevoda

Head of Banking Regulations Division Credit Institutions Supervision Department